

Annual Report

For Year Ending

December 31, 2003



The Alberta Automobile Insurance Board, constituted under subsection 653(1) of the *Insurance Act*, is empowered under section 654 thereof to investigate any matters it thinks fit respecting automobile insurance in Alberta, and to approve rates charged by insurers for compulsory automobile coverage under the *Motor Vehicle Administration Act*, replaced by the *Traffic Safety Act* in May 2003.

RATES

Insurers conducting business in Alberta are required by the *Insurance Act* to report their experience to a Canadian statistical plan. The results are compiled annually in Insurance Bureau of Canada published statistical exhibits that are then analyzed by the Board's actuarial consultant. The most recent available results are for 2002. These analyses are used in weighted proportions with the insurers' own statistics and analyses performed by insurers' underwriting groups in considering proposals for rate changes.

A pattern of deteriorating results that emerged in the mid 1980s sustained itself through to the present, particularly for Private Passenger vehicles. The phenomenon is attributable to the growth in compensation for bodily injury claims under third party liability and, to some extent in more recent years, under accident benefits coverage. Premiums for third party liability and accident benefits rose steadily through the 1990s in response to rising claim costs, though competition tempered the process. The premium growth trend tapered off during 1999 and 2000 but resumed in 2001. Pricing for all categories of general insurance hardened in the latter part of 2001 and that course continued through 2002 and 2003.

MARKET

Premiums for third party liability and accident benefits on Private Passenger vehicles continue to increase in response to claims experience. The escalation in premium abated somewhat during 1999 and 2000 but insurers strove for premium adequacy from the latter part of 2001 until the Government imposed a rate freeze effective October 30, 2003. In contrast, collision and comprehensive coverage have yielded satisfactory results since the mid 1990's. This phenomenon has in part offset adverse results for third party liability and accident benefits.

Third party liability encompasses bodily injury and property damage. The area of concern for many years has been the persistent spiral in both average cost and frequency of bodily injury claims, though frequency appears to have levelled off. It takes a number of years for third party liability bodily injury claims incurred in a given year to mature. Therefore, results for recent years are projected to their expected ultimate values based on historical observations of the maturation of such claims. Expectations are that over the five years ending in 2002, the average compensation for a bodily injury claim will have increased 16% while frequency of this type of claim will have increased by less than 1 percent. The climb in settlement amounts and relatively stable frequency combines for a 17% increase in the claim cost per vehicle insured. The steady rise in frequency that peaked in 1998 has since remained relatively stable. In comparison, the average property damage claim will have increased by 26% while frequency of this type of claim will have actually fallen by 7 percent. For property damage, the claim cost per vehicle insured will have increased by 18 percent. Figures 1 and 2 track the changes in average claim costs and frequency of claims for a longer period of ten years ending in 2002. Figure 3 displays loss costs per vehicle insured, which are total losses divided by the number of vehicles insured. The

figure relates the combined effect of average claim cost and frequency. Declining frequency of property damage claims continued to partially offset increasing average claim costs.

Over the past five years, the overall effect for third party liability coverage is a 23% growth in the average claim size while frequency will have declined 5 percent. The claim cost per vehicle insured will have increased by 17 percent. Bodily injury is expected to comprise 81% of total third party liability claim costs for 2002, similar to the percentage for 1997. Figure 4 shows the change in average claim costs and frequency of third party liability claims over a longer ten year period.

Rising average claim costs has affected accident benefits in recent years. In the five years ending in 2002, the average claim cost will have increased by 18% while frequency of this type of claim decreased by 3%, having moderated slightly after peaking in 1998. The claim cost per vehicle insured will have risen 14 percent. Figure 5 shows the change in average claim costs and frequencies of claims over a longer ten year period. Compensation available under accident benefits coverage doubled for losses occurring as of October 1, 1995, contributing to increased average claim costs since 1996. There is a partial offset as the compensation is deducted from any third party liability claim.

Frequency for collision claims diminished for a number of years but has fluctuated over the past five years. Frequency of comprehensive claims continues to diminish. Over the same five year period, the average claim cost for collision will have increased by 32% while frequency will have increased 3 percent. The claim cost per vehicle insured will have increased by 35 percent. The average claim cost for comprehensive will have increased by 69% while frequency will have dropped 34 percent. The claim cost per vehicle insured will have

increased by 12 percent. There have not been any weather related catastrophes that significantly impacted results. Figures 6 and 7 show the change in average claim costs and frequencies of claims over a longer ten year period. In summary, Figure 8 shows loss costs per vehicle insured for each coverage. All costs are in nominal dollars (unadjusted for inflation).

The standard market's criteria for acceptable risks respond to results. As loss experience improves, the underwriting criteria relax and more drivers gain access to the standard market. Criteria become more stringent as results deteriorate. A tightening of the market was apparent in the latter half of 2001 and continued through 2003.

Drivers with no recent losses or convictions can readily access the standard market. However, the industry that had once competed with abandon for those drivers with a clear record for the past six or more years has changed their focus from market share to adequacy of pricing. Access to markets was traditionally more limited for drivers with some recent frequency of claims and convictions. These drivers are channelled into residual or non standard markets at higher premiums. The choice and more competitive pricing for these drivers that came with the expansion of this market segment prior to 2001 has suffered some reversal with the decision of some of these markets to limit their activity.

The Facility Association is the industry's mechanism for providing insurance to those consumers who are refused coverage elsewhere. The Board monitors the Association's program for all coverage. Their share of the Private Passenger market peaked at 6.5% for 1992. Market share dropped to 6.0% for 1993 and continued its decline to .94% for 2000. The trend reversed in 2001 with a slight increase to .96% of written vehicles and climbing to 1.3% for 2002. Though firm

numbers are not yet available, it is evident that market share increased further in 2003.

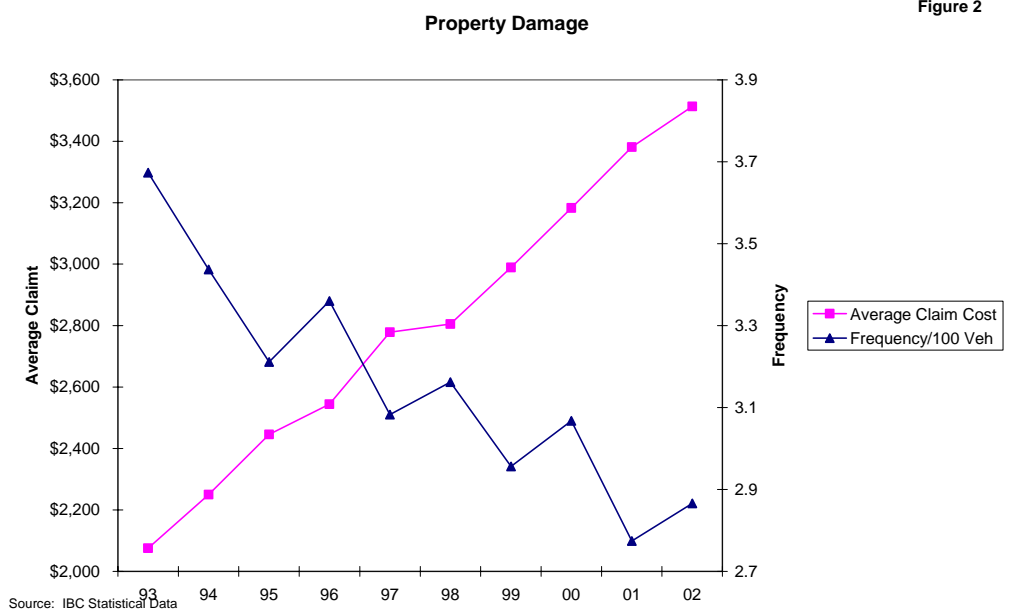
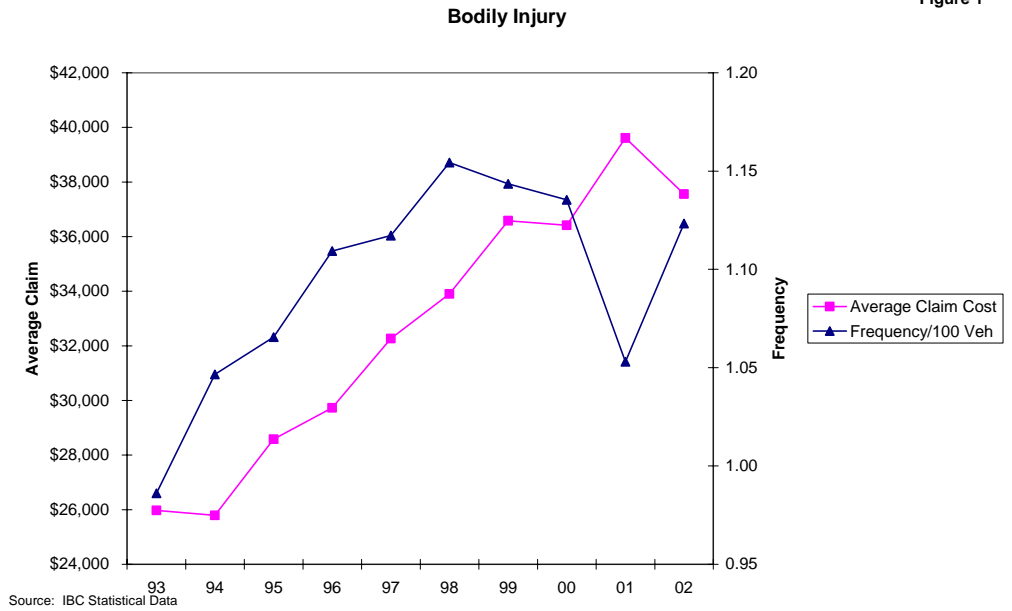


Figure 3

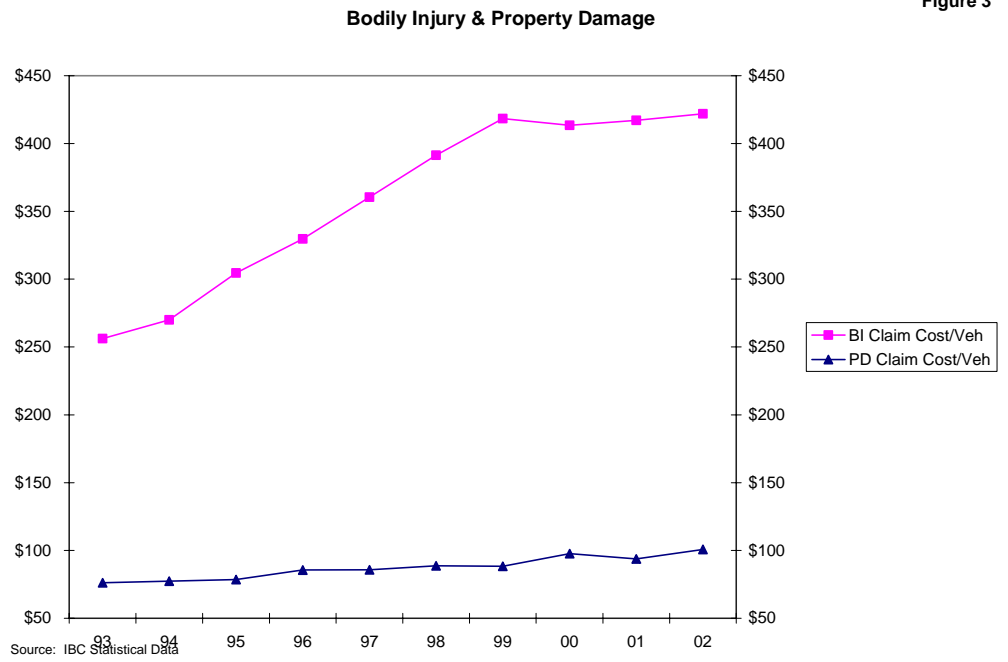


Figure 4

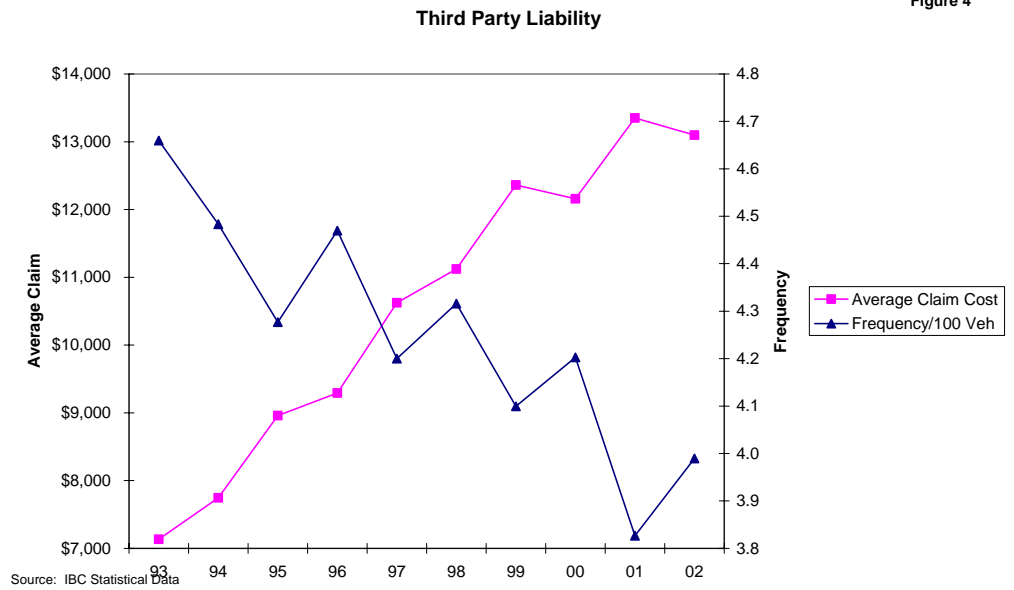


Figure 5

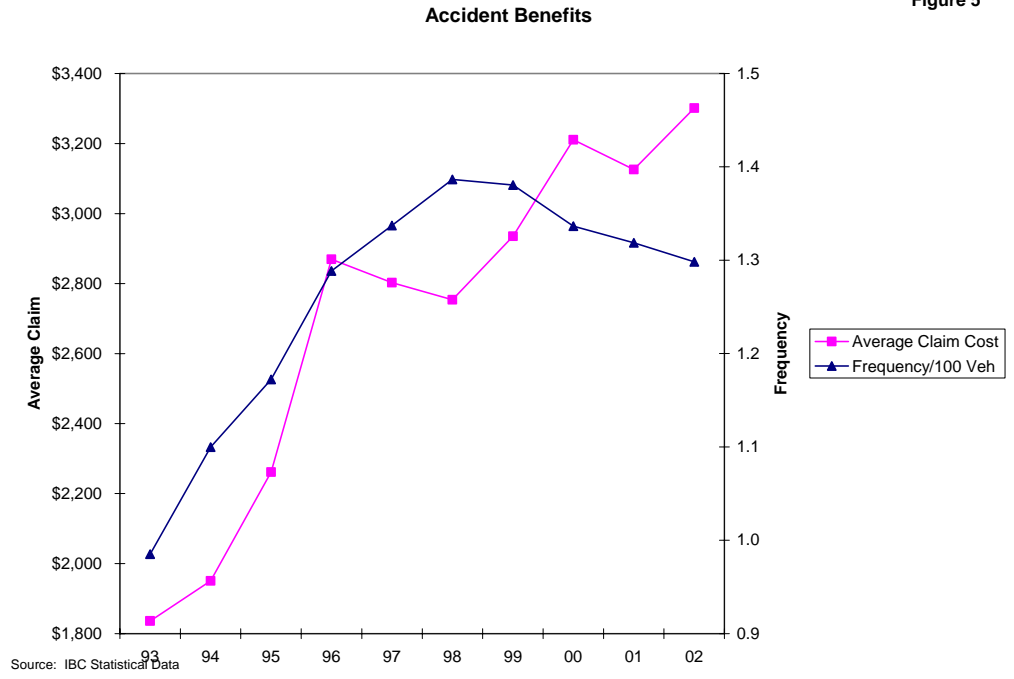
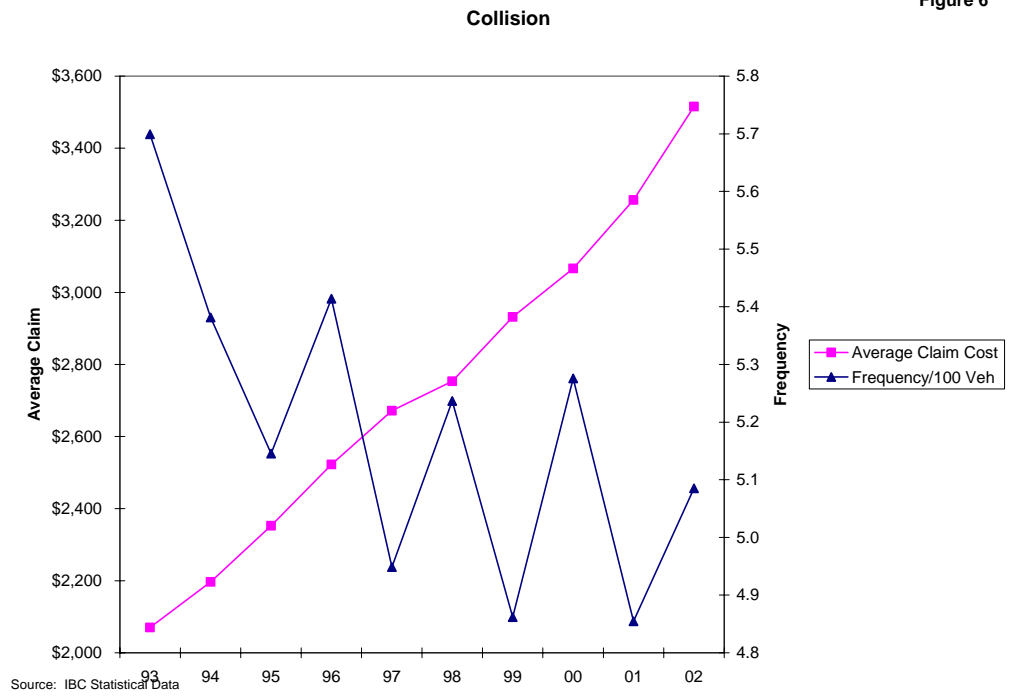
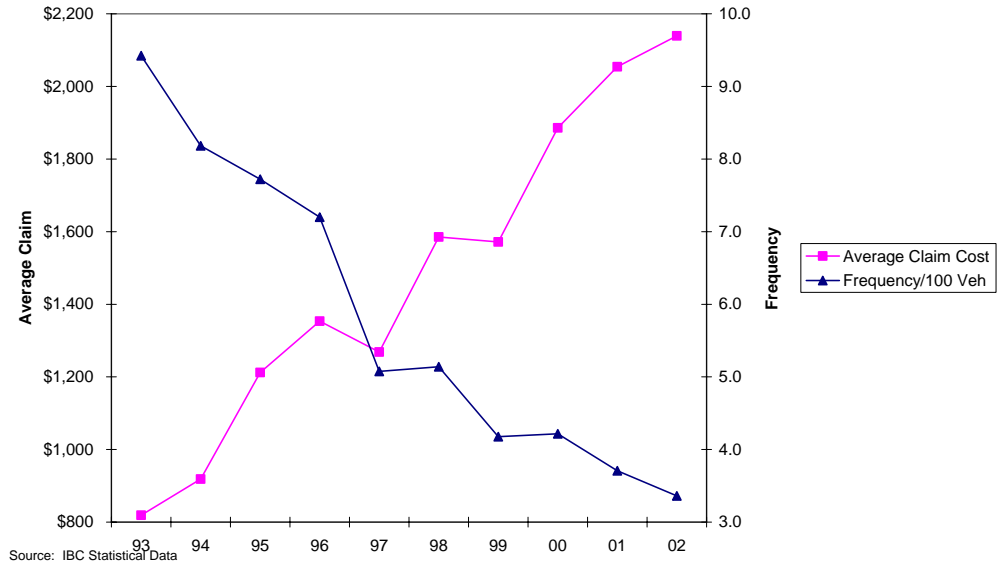


Figure 6



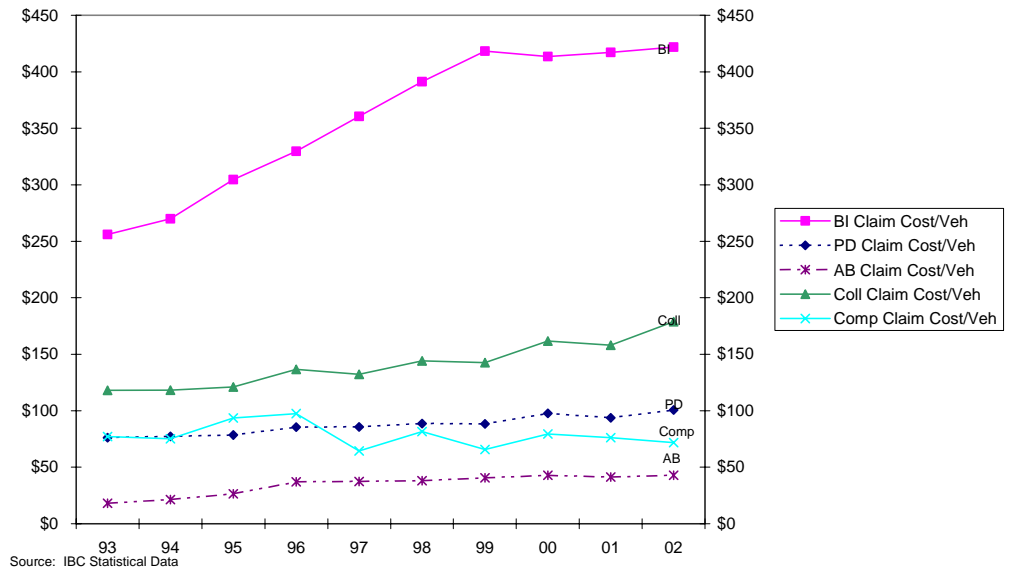
Comprehensive

Figure 7



Claim Cost Per Vehicle Insured

Figure 8



INQUIRIES

Inquiries and complaints are monitored for unfair and inequitable rules and practices. Complaints are assessed for compliance with rates and rules, and are resolved through representation to the insurer or provision of a detailed explanation. The Board office received 397 inquiries in 2003.

BENEFITS

The current compulsory third party liability limit of \$200,000 places Alberta at a level at least equal to any other Canadian jurisdiction. However, the Board recognizes the critical importance of adequate limits and continues to maintain its recommendation of a compulsory limit of at least \$300,000 that would involve an increase of up to 9% to the premium. An increase to \$500,000 would involve an increase of up to 18% to the premium for current minimum limits.

MEETINGS

In 2003, the Board held 9 meetings during which 112 applications were examined. This number compares with 157 applications in 2002, 149 in 2001, 127 in 2000, 123 in 1999 and 128 in 1998. Seven applications were declined of which four were subsequently revised and approved and one approved on appeal. Thirty-seven of the applications were approved subject to modifications.

LIAISON

The Automobile Insurance Board attempts to meet with executive members industry associations in order to maintain dialogue with the industry's various component groups. In 2003, they met with the Independent Insurance Brokers Association of Alberta (IIBAA) and a number of insurers.

STAFF

Susan Steeves is Administrator to the Board.

MEMBERSHIP ON THE BOARD

There were no changes during 2003.

GENERAL

Background

This is the final Annual Report of the Alberta Automobile Insurance Board. The Board operated from 1971 through 2003, ensuring reasonable automobile insurance pricing for third party liability and accident benefits coverage and examining pertinent issues relating to automobile insurance. The Board monitored the automobile insurance industry and alerted Government to emerging issues and developing crises.

In the face of a collapsing residual market system, one project was the study of alternative systems and the recommendation to adopt the current Facility Association plan. Similar dysfunction elsewhere

resulted in the simultaneous implementation of Alberta's solution in all private delivery jurisdictions.

Another effort was the conduct of public hearings and issuance of a report on the issue of age, gender and marital status as rating criteria for automobile insurance. The 1985 report found the criteria to be credible predictors of risk. The conclusion received further corroboration in 1992, when the Supreme Court of Canada reached a similar decision and in 1993, the Alberta Court of Appeal ruled that use of gender as a rating criterion is reasonable and justifiable.

Possibly the most notable undertaking was "A Study of Premium Stability in Compulsory Automobile Insurance" completed and submitted to Government in 1991. As was the case in 2002 and 2003, the beginning of the 1990s brought rapidly increasing premiums in response to escalating bodily injury loss costs and restrictive underwriting practices that resulted in substantial growth in market share for the non standard market. That document has served as a point of reference for other jurisdictions facing similar predicaments and for those attempting to secure modifications to the current system of compensating claims for bodily injury sustained in automobile collisions.

Preparation of the report included a closed claim study that indicated that those individuals with less serious injuries were over-compensated relative to those individuals with more serious injuries. That was not to say that any injured person does not deserve compensation. Rather, if the funds to compensate were not limitless, then some measures were needed to control the compensation for less serious injuries in an effort to control costs and achieve a more effective distribution of available resources. Most of the growth in bodily injury loss costs were attributable to the non-pecuniary general damages component of claims, which were found at that time to

comprise about 48% of all bodily injury claims compensation, but 83% of dollars awarded for minor claims.

The report and, therefore, the Board, concluded there was no specific feature operating in the current system to control increases in claims costs. The Board expected loss costs would continue to increase in the long term unless bodily injury costs were curtailed in some fashion. They examined the effect of tort reform, an alternative threshold no-fault system and enriched no fault accident benefit provisions on loss costs and the impact on premiums.

The report emphasized the need for effective government measures to reduce severity and frequency of accident costs. The report opined that reduction of the causes of those costs should be a priority, irrespective of any modification of the automobile insurance system. The following is that list of recommendations, some of which have since been acted upon in some measure:

- a. set up a coordinated approach to traffic safety and carry out a unified policy of safety measures to reduce traffic accidents in Alberta.
- b. engage police in a year round program of primary enforcement of the seatbelt law.
- c. support federal authority responsible for vehicle safety standards requiring airbags and automatic restraint systems in new vehicles.
- d. double penalties for unsafe speed and other traffic offences most often committed in injury accidents.
- e. reassess the use of police resources in urban and rural areas to target and increase enforcement of offences involving large deviations from average traffic speeds and those offences most often correlated with injury accidents.
- f. upgrade the Check Stop program, by the following:

- (i) promoting the authorization of police to administer breath tests to all drivers,
 - (ii) targeting night-time hours, and rural areas,
 - (iii) operating it more frequently during the year and,
 - (iv) publicizing the added enforcement features and results for violations.
- g. carry out a graduated licensing program for new drivers.
 - h. make greater use of short term licence suspensions.
 - i. study the feasibility of raising the minimum legal age for consumption of alcohol.
 - j. study the feasibility of driver safety education programs for school age children to foster appropriate attitudes at an early age.
 - k. study the feasibility of effective rewards to engender greater care in driving.
 - l. require insurers to show rate rewards and disincentives on automobile policies.
 - m. study the feasibility of raising the minimum legal age for driving.
 - n. study effective methods for improvement of highway design and conditions especially in rural areas.
 - o. investigate the feasibility of setting up trauma and improved rehabilitation centres.

Traffic Safety

Traffic Safety has been a recurring topic in the Board's Annual Reports. Logically, a reduction in the number and severity of injuries would have a positive effect on rising loss costs, not to mention the human toll. The Board was encouraged by the growing and sustained interest in traffic safety programs over the past decade. The Government's "Think and Drive" continues to bring the traffic safety issue into the public forum. The Board recognized "Mission Possible" sponsored by a coalition of insurers and other partners, including

government, with a vested interest in traffic safety as a significant endeavor. The Royal Canadian Mounted Police (RCMP) demonstrated the need to focus on traffic safety issues in rural areas of the province, where their organization principally operates. Convinced of the gravity of the situation, the Board formally endorsed their traffic safety education and enforcement program.

Premium Stability

Injury claims remain the root cause of the escalation in third party liability premiums. The section on Market details recent history. Developments are consistent with the Board's earlier conclusion that there is nothing operating in the current compensation system to control bodily injury claim costs.

The Insurance Bureau of Canada has continued to pressure for various measures of tort reform. The Board supported efforts toward tort reform that would serve to temper injury claim costs. Bill 53, passed in December 2003, promises some measures to address overpayment of lost income and potentially place some control on non-pecuniary damages for minor injuries.

Until the latter half of 2001, the market had remained competitive for drivers with acceptable driving records and improved for what had been an under serviced non standard market. Accumulated deficiency in pricing combined with continuing deterioration in claims experience that was further exacerbated by diminished investment return forced insurers to shift their focus from market share to bottom-line considerations. The steps initiated in the late stages of 2001 continued through 2003. The restrictions in market and escalation in premium were not peculiar to the automobile sector of general insurance. There are faint indications that the market could begin to improve over 2004 for at least some lines of business.

The previous Annual Report related that recent increases in premium level for automobile insurance coverage and the virtual certainty that the trend would persist raised questions regarding continuing affordability of coverage for a segment of the driving public. In turn, there was cause for concern as to whether the issue of affordability could aggravate the incidence of uninsured vehicles.

The Government moved to freeze automobile insurance premiums as of October 30, 2003. The freeze is intended to provide some relief while Government completes development of and implements its automobile insurance reform package. As well as taking steps to limit claims costs for minor injuries, they intend to establish a benchmark premium schedule that establishes the maximum premium for third party liability and accident benefits coverage that can apply to a driver profile. In an effort to stem the flow of risks to Facility Association, a regulation was established in December 2003 to limit insurers' ability to decline coverage.

The automobile is a pervasive and very important element of today's lifestyle. The fact that it impacts a vast majority of the population has rendered automobile insurance a highly charged issue. A stable environment is critical to all stakeholders including insurers, Government and, of course, Alberta motorists. Achieving that end requires a reasoned, consultative reform process that appreciates the expectations and requirements of the various parties. The cyclical nature of the insurance industry means that some of the problems of the past couple of years would recede with the passage of time. There are other shortcomings that do require remedy and the judicious resolution of those deficiencies will serve to ease the impact of future hard market conditions.